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Submitted electronically

Dear Commissioners

ERC0302 – Deferral of Network Charges

EnergyAustralia is one of Australia's largest energy companies with around 2.5 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market (NEM).

We appreciate the opportunity to provide comment on the AER initiated rule change for the Deferral of Network Charges. We understand the purpose of the rule is to support retailers, where required because of COVID related cash flow impacts (specifically customer payment plans, deferrals and inability to pay), to support customers.

COVID-19 impacts

The impacts to customers from the COVID-19 pandemic have been noticeable but not systemic. There is a growing financial impact apparent in increased customer support required and a corresponding reduction in retailers' cash-flow. EnergyAustralia supports whole of industry measures that assist retailers in supporting households and businesses doing it tough.

Retailers acted early in supporting customers impacted by the COVID pandemic through both hardship programs and tailored assistance. Retailer's minimum hardship policy requirements are outlined in the AER's Hardship Policy Guidelines[1], some retailers exceed the AER requirements. These requirements are the highest level of standards available to Australian customers in any industry.

The support retailers are providing has resulted in an increase in customers receiving assistance under their respective hardship programs; including deferral of payments and payment plans. However, the financial impacts (cash flow & bad debt) to retailers from COVID has probably not yet fully materialised, as customers have received government assistance via JobKeeper and the increases to JobSeeker.

[1] https://www.aer.gov.au/retail-markets/retail-guidelines-reviews/customer-hardship-policy-guideline

EnergyAustralia anticipates a foreseeable risk of financial problems emerging in Q4 2020; when the government assistance packages and the bank's mortgage deferrals expire. We understand the intent of the AER rule change is to provide support to retailers sufficient to help customers as the economy restarts. However, the form of support required by customers depends on the nature of the recovery; v, u or otherwise. This is not yet known, which means policymakers should consider a rule which allows for different forms of recovery.

Effective and targeted retailer support

EnergyAustralia is concerned that limiting the retailer support to solely a deferral of network charges may not be sufficient to meet the intent of assisting customers in all circumstances.

EnergyAustralia suggest the AEMC consider expanding the rule to be flexible to the uncertain future the industry is facing. EnergyAustralia suggest the AEMC should amend the rule to determine eligibility based on debt thresholds; triggered where a retailer's unpaid debt is above a % threshold:

- The AER can track each retailer customer debt levels against historic outcomes and estimate the levels at which a retailer can maintain financial viability.
- Where a threshold debt level is triggered, exceeding historic outcomes by a margin and creating cash flow demands, the network charge deferral could be applicable.
- Where a higher threshold of debt is reached that threatens retailer viability, there could be a second intervention with networks bearing the bad debt risk and rebating their portion of the unpaid network bill; perhaps this could be linked to where a customer on a retailer's hardship assistance program has ultimately not paid and retailers have been required to waive the debt.

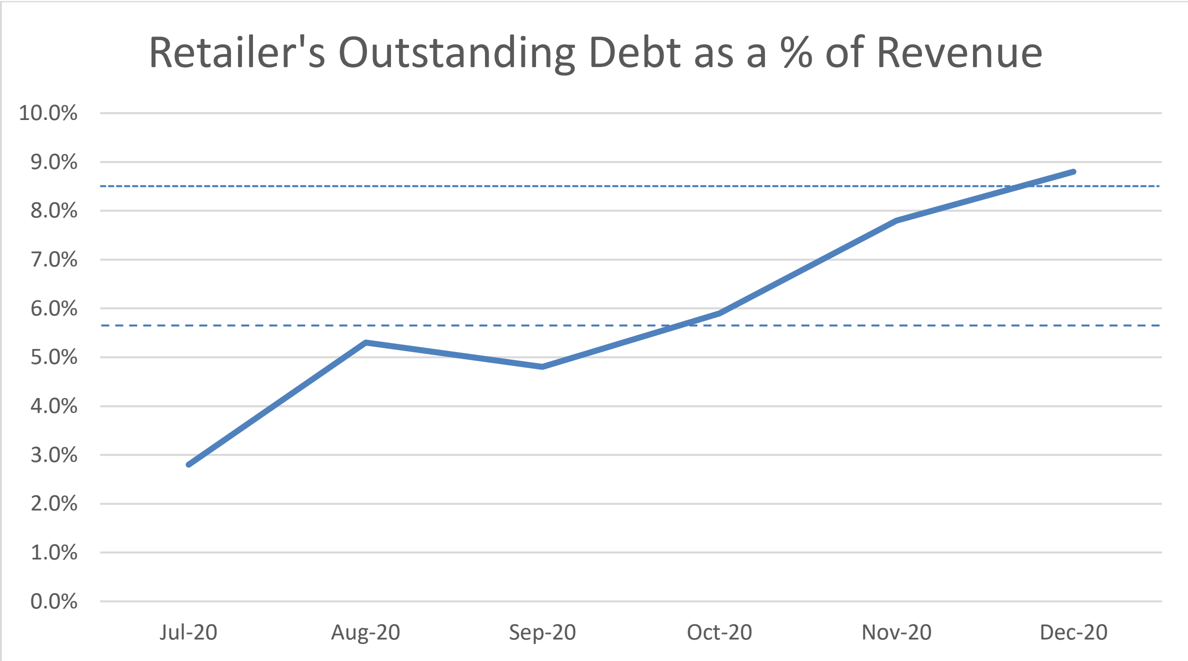
The AER should consider basing the thresholds for retailer assistance on retail operating margins. The ESC determines retail operating margins in its determination for the VDO; *Retail operating margin represents the operating profit margin required to compensate investors for the capital provided to operate a retail service. It should be sufficient to cover the cost of capital, and the systematic (non-diversifiable) risk associated with investment. The retail operating margin is expressed as a percentage of the cost stack*[2].

The ESC determined that the 2020 VDO would have a retail operating margin of 5.7%[3]. Assuming that this operating margin is a rough proxy for the cash generated from retailing, then EnergyAustralia suggests the thresholds for assistance could be based around this magnitude of cash impact. For example:

1. If, a retailer's outstanding debt is ≥5.7% of the retailer's revenue (roughly implying no cash is being generated by the business), the network charge deferral applies;

[2] https://www.esc.vic.gov.au/electricity-and-gas/prices-tariffs-and-benchmarks/victorian-default-offer/victorian-default-offer-price-review-2020 Final Decision, Section 3.6 pg. 50-51
[3] https://www.esc.vic.gov.au/electricity-and-gas/prices-tariffs-and-benchmarks/victorian-default-offer/victorian-default-offer-price-review-2020 Final Decision, pg. 59

2. If, a retailer’s outstanding debt is ≥8.5% of the retailer’s revenue (roughly implying the impact is 1.5x the expected cash generation of the business, meaning retailing businesses will be facing challenges in how to manage working capital), the networks charge rebate for customers receiving hardship assistance could apply.



The rule could allow the AER to alter the specific debt threshold trigger for each level of assistance (deferral or rebate) and extend the duration of the assistance based on the fluctuating and evolving nature of the economic recovery following the COVID pandemic.

Note that some debt metrics for retailers are already being reported to the AER and changes in these numbers will be visible through this data.

Supporting retailers to support customers

The AEMC’s proposed rule is to support retailers, thereby supporting retailers’ customers; limiting the support to smaller retailers is against the intent of supporting all customers.

EnergyAustralia expects the limited timeframe available for to the AER to implement the rule will place a constraint on their capacity to effectively assess retailer eligibility; however, we believe that it will be best tailored by applying the rule automatically based on a retailer’s outstanding debt balances. This assessment will ensure that any retailer that is facing increased financial difficulty due to COVID-19 pandemic will receive assistance – allowing them to continue to support customers.

Fair and equitable support to retailers

When the deferral on network charges concludes there will be many customers with larger debt balances than they have ever had before. It is a fundamental responsibility of Retailers to support customers that are experiencing difficulty in managing their energy affordability; however, this responsibility comes with associated risk. The allocation of risk that has historically been considered the remit of retailers, was not established to handle the financial crisis resulting from the COVID-19 pandemic.

EnergyAustralia believes that at the conclusion of the network charge deferral it is still likely that retailers will be financial vulnerable from COVID-19 impacts, and as such the AEMC should potentially consider further changes towards the end of 2020. This could consider for example whether network cost deferrals have been effective in solving cash flow challenges for retailers and enabling customer support – or whether network rebates might be required to meet the objectives of the rule.

The amounts that are forfeited by networks could be supplemented by future adjustment to correct lost revenue, through network determinations; conceivably this would be done over the four-year determination period, or longer, to lessen the effect on price increases.

We believe that measures to support retailers should not be limited to electricity, and that the AEMC should consider expanding the rule to cover gas networks. The easing of restrictions may ease some of the increased consumption that customers have incurred during the stricter social distancing requirements; however, it is expected that winter gas bills will still be noticeably higher.

If you would like to discuss this submission, please contact me on 03 8628 1704 or Travis.Worsteling@energyaustralia.com.au.

Regards

Sarah Ogilvie

Industry Regulation Leader

AEMC

ATTACHMENT 1
STAKEHOLDER FEEDBACK TEMPLATE

The template below has been developed to enable stakeholders to provide their feedback on the questions posed in this paper and any other issues that they would like to provide feedback on. The AEMC encourages stakeholders to use this template to assist it to consider the views expressed by stakeholders on each issue. Stakeholders should not feel obliged to answer each question, but rather address those issues of particular interest or concern. Further context for the questions can be found in the consultation paper. Stakeholders are also encouraged to provide evidence to support claims where possible.

SUBMITTER DETAILS

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CHAPTER 4 – SECTION 4.1 – THE PROBLEM - IMPACT OF COVID-19 ON THE RETAIL ELECTRICITY MARKET

Question 1 – Impact of COVID-19 on retailers	
a) What is the expected impact of COVID-19 on retailers' cash flows? How material is this impact? How long are these cash flow impacts expected to last?	Everyone has been impacted by the COVID pandemic; retailers are certainly not immune, with long-term hedging impacted by reductions in forecast demand, workforce and productivity limitations due to mandatory social distancing, and a significant increase in customers seeking support. The cash flow impacts to EnergyAustralia are presenting in a 60% increase in residential customers seeking support. We have not yet experienced the systemic issues we anticipated, and we believe the true extent of the COVID impacts will not be seen until Q4 2020; when govt assistance (JobSeeker & JobKeeper) and mortgage deferrals expire.
b) In the absence of the proposed rule change, what options are available to retailers to manage the cash flow impacts of COVID-19? Are existing support schemes that have been announced, including the Network Relief Package, sufficient to assist retailers to manage these impacts? If not, what are the areas where further assistance is needed?	Retailers could seek assistance from instititutions, shareholders, government, or parent companies (dependent on their structure); however, each of these options will have differing capacity for application in ease and timeliness, and will be subject to the changing nature of the pandemic and the specific level of assistance required. A preferable rule change would apply assistance to retailers based on merit (not a subjective assessment of 'size') and will enable additional assistance if required to address the bad debt incurred by retailers. EnergyAustralia believes that a threshold limit comparing outstanding debt to a retailer's revenue, will provide targeted assistance to retailer's that are in need of assistance; as retailers will have limited or no cash if outstanding debt exceeds their profit margin. The ESC's 2020 VDO determination has set the retail operating margin at 5.7%[1]; therefore, it is reasonable to set the initial network charge deferral threshold to commence if a retailer's outstanding debt is ≥5.7% of the retailer's revenue. EnergyAustralia suggest that further assistance could include networks rebating their portion of a retailers hardship customers, if a retailer's outstanding debt ≥8.5% of the retailer's revenue (roughly implying the impact is 1.5x the expected cash generation of the business, meaning retailing businesses will be facing challenges in how to manage working capital).

[1] https://www.esc.vic.gov.au/electricity-and-gas/prices-tariffs-and-benchmarks/victorian-default-offer/victorian-default-offer-price-review-2020 Final Decision, pg. 59

c) What are the expected impacts of the proposed rule change on any cash flow issues currently being experienced by retailers as a result of COVID-19?	The proposed rule change would eleviate a portion of the immediate cash flow impacts of retailers, this will be beneficial as it addresses a significant cost area; network payments. However, the proposal only addresses the short-term cash-flow support of retailers, we believe that the immediate assistance this provides to retailers will not remove the underlying problem, of significant bad debt. The effectiveness of the AER package derives from the assumption that Australia is now able to manage the spread of the virus and therefore can restart many businesses that were hibernating; the economy then achieving a v-shaped recovery. EnergyAustralia is concerned that a deferral of charges is short-sighted to the economic ramifications that have been created by the COVID-19 pandemic. The indicators of a weak economy were present prior to the emergence of COVID-19, it is therefore expected the recession[2] that COVID-19 started will follow a u-shaped recovery; employment, GDP, and industrial output sharply decline and then remain depressed typically over a period of 12 to 24 months. As such, any intervention timeframe should be extendable based on the AER's assessment, which can be determined via the information it is able to access by its regulated right to participant data. The ENA Relief Package provided smaller retailers (defined by the ENA) a waiver of charges and to large retailers a deferral of network charges for COVID impacted customers experiencing financial difficulty. The AER Statement of Expectation required a ban on disconnections amongst other requirements to protect customers impacted by the COVID crisis. The consequence of these packages to customers of large retailers is that this has enabled their debt to significantly increase. When the deferral on network charges concludes there will be many customers with larger debt balances than they have ever had before.

[2] https://www.abc.net.au/news/2020-06-05/coronavirus-recession-not-like-others/12322182

CHAPTER 4 – SECTION 4.2.1 – ELIGIBILITY TO DEFER PAYMENT OF NETWORK CHARGES

Question 2 – Retailer eligibility	
a) Is it appropriate and/or necessary to expressly exclude certain classes of retailer from deferring the payment of network charges under the proposed rule change? If so, please provide reasoning to support your position.	The deferral of network charges for customers impacts by COVID will not materially impact networks, if assistance is only provided to retailers that exceed a threshold that enables the assistance to be provided. Excluding a class of retailer without an assessment of merit will place additional risk on these retailers and their customers. EnergyAustralia acknowledges that small retailers are facing increased financial difficulty and reduced cash-flow, resulting from COVID-19. This is a reality of all retailers, to only consider the needs of smaller retailers will create a disparity in the market, which will have adverse impacts later: • Extended viability of retailers that were in financial difficulty prior to the COVID-19 pandemic, which will continue to unviable upon completion of the support package. • Large retailers bearing the cost of supporting customers through the proposed support package, with the financial impacts culminating for large retailers at a period when customer support is reduced or no longer available. • Damage the competitiveness of the retail market by promoting a perception that customers of large retailers would receive better support at a small retailer.
b) If the onus is placed on retailers to show they have a legitimate financial need to access the proposed deferral mechanism, what eligibility criteria should apply?	As above, we do not support the package being applied to only retailers that have an immediate financial need. Any eligibility criteria should consider the bad debt impacts retailers are forecast to experience as a result of assisting customers through the COVID crisis. 1. If, a retailer's outstanding debt is ≥5.7% of the retailer's revenue (roughly implying no cash is being generated by the business), the network charge deferral applies; 2. If, a retailer's outstanding debt is ≥8.5% of the retailer's revenue (roughly implying the impact is 1.5x the expected cash generation of the business, meaning retailing businesses will be facing challenges in how to manage working capital), the networks charge rebate for customers receiving hardship assistance could apply.

c) What would be an appropriate and efficient process for the verification of information provided by retailers under the approach described in (b) above?	Retailers provide the AER with their preference of weekly/fortnightly/monthly reporting to establish their eligibility for any assistance. The retailer's reporting indicates how the retailer operating margin (or profitability) has been impacted by outstanding customer debt.
d) Do stakeholders have views on how the deferral mechanism could be designed to incentivise only those retailers that legitimately require immediate financial support due to COVID-19 to access this mechanism (including allowing DNSPs to charge interest on deferred payments)?	If the deferral mechanism is only applied to retailers that have exceeded the threshold limits, it will limit the application to only retailers that are in need. There would be no incentive for retailers to try to reach the threshold limit, as this would result in their business being unprofitable.
e) Do stakeholders have views on whether any of the approaches outlined above (or a combination of each) would be preferable?	EnergyAustralia's preference is that all retailers are considered based on their need, and that additional assistance by way of networks rebating their charges be considered if required; i.e. when a retailers outstanding debt is ≥8.5% of the retailer's revenue.

Question 3 – Customer eligibility	
a) Do stakeholders have views on the types of customers that should be captured by the proposed deferral mechanism and how these customers can be clearly defined in the NER? Is it appropriate and/or necessary for this mechanism to include large commercial and industrial customers?	The AER's hardship guidelines[3] provide the minimum requirements for entry to retailers' hardship programs, these requirements are suitable for effectively covering the scope of customers that should be considered under this mechanism. This is something that retailers already comply with, therefore there is no additional analysis or resourcing required to provide this confirmation to networks. EnergyAustralia believes this support should include all customers that are experiencing financial difficulty as a result of the COVID crisis, this includes customers that were experiencing financial difficulty prior to the pandemic, SME, and C&I. This may be viewed as a broad brush; however, if we are considering this mechanism as a way to support retailers from cash flow impacts, the cash flow impacts are spread across all these customers.

[3] https://www.aer.gov.au/retail-markets/retail-guidelines-reviews/customer-hardship-policy-guideline

CHAPTER 4 – sECTION 4.2.2 – DEFERRAL TIMEFRAME AND TERMS

Question 4 – Length of deferral period	
a) Is a six-month deferral of the payment of network charges an appropriate timeframe, having regard to the potential cash flow impacts of COVID-19 on the retail electricity market in the second half of 2020? Alternatively, would a shorter deferral timeframe be sufficient to allow retailers to overcome the financial pressures posed by the current environment?	EnergyAustralia forecast the impacts of COVID to be more pronounced in late 2020, when the government grants (JobKeeper & JobSeeker) and mortgage deferrals are wound up. Therefore, a six-month deferral should be provided at a minimum, with the capacity for the mechanism to be extended where required.
b) What are the implications (if any) of a six-month deferral period for NSPs, compared to a shorter or longer deferral period?	Networks should consider that without supporting retailers, there is the possibility of a worst-case scenario in which there are multiple ROLR events; this will result in significant unpaid amounts to networks, whereas the proposed mechanism is only deferring the payment. Networks will not want to have any 'skin in the game', which is understandable considering their position in a BAU world, what should be considered by the AEMC is that this is not a BAU world, there are positive signs of recovery; however, even with a v-shaped recovery, we are likely to see significant economic impacts for the foreseeable future, which are culminating at a time where retailer viability was already under pressure from regulated pricing (VDO & DMO). Retailers accept and appreciate their role in supporting customers that are experiencing difficulty in managing their energy affordability, this has been a fundamental responsibility since the privatisation of the energy industry; however, this responsibility – allocation of risk – was not established to handle the financial crisis resulting from the COVID-19 pandemic. If networks (DNSP & TNSP) are not required to reconsider the allocation of risk, the AER and ENA's packages of customer support will be in vein. EnergyAustralia believes that at the conclusion of the network charge deferral it is still likely to result in the loss of retailer (small and/or large) financial viability. EnergyAustralia suggest the AEMC consider expanding so that if a retailer's outstanding debt is ≥8.5% of the retailer's revenue the network would rebate their portion of the unpaid network bill; where a customer on a retailer's hardship assistance program has ultimately not paid and retailers have been required to waive the debt. The amounts that are forfeited by networks could be supplemented by future adjustment to correct lost revenue, through their network determinations; conceivably this would be done over the four-year determination period, or longer, to lessen the effect on

	price increases. This would be a vital step in ensuring that retailers are able to survive the financial impacts of the COVID pandemic. The alternatives of an increased deferral period, or to continue with the status quo, are likely to have a similar result; retailer failure. Networks will argue that the allocation of risk should not change, despite the adverse impacts of retailer failure being far greater to a network; loss of all un-paid network payments when a retailer becomes insolvent, compared to absorbing their portion of a minority of a retailer's customers that have not paid, which they will ultimately be able to recover.

Question 5 – Extension of deferral period	
a) Is it appropriate and/or necessary for the AER to have the ability to extend the deferral period if this is considered necessary? If so, what conditions, considerations and/or consultation requirements should reasonably apply to the exercise of this power?	As the forecast climax of the financial impacts is not expected until Q4 2020, the AER should strongly consider the ability to extend the deferral period.

CHAPTER 4 – SECTION 4.2.3 – DEFERRAL OF PAYMENTS BETWEEN DNSPS AND TNSPS

Question 6 – Deferral of payment of transmission network charges	
a) Is it necessary and/or appropriate for DNSPs to be able to defer the payment of transmission charges to TNSPs under the proposed deferral mechanism? To what extent would this change the overall impact of the proposal on DNSPs? What would the impact of this approach be on TNSPs?	EnergyAustralia believes it is reasonable for the payment deferral mechanism be extended to include DNSPs payments to TNSPs.
b) Do stakeholders have views on how the deferral of payments from DNSPs to TNSPs would be implemented in practice? What issues would need to be addressed in the regulatory framework to facilitate this?	

CHAPTER 4 – SECTION 4.3 – PRACTICAL IMPLEMENTATION OF PAYMENT DEFERRALS

Question 7 – Process for deferring payment of network charges	
a) Do stakeholders have views on appropriate processes which could be adopted to facilitate the proposed payment deferrals in an expedient manner?	EnergyAustralia believes the process currently required by the VIC networks for the ENA Package is the preferable process to facilitate the payment deferral; the VIC distributors process accepts that retailer's assessment of a customer requiring assistance, therefore is not burdensome in a request for substantiation.
b) Could the processes agreed between retailers and NSPs for implementing the Network Relief Package also be used to implement the AER's proposal?	As above, retailers and networks have implemented a process resulting from the ENA package. It would be efficient to continue with these functioning processes; however, our preference is that all networks adopt the VIC networks process, as it is the most efficient in providing the required information to networks, and there will be increased efficiency in streamlining the process across networks.
c) If the details of this process are not prescribed in the NER, what alternative approaches would ensure that the payment deferrals could be administered in a transparent, consistent and efficient manner? Is it feasible for the details of this process to be directly agreed between NSPs and retailers?	EnergyAustralia believes that it is not required for the process to be prescribed in the NER, as with the ENA package an agreement can be directly agreed between networks and retailers.

CHAPTER 4 – SECTION 4.4 – IMPACT ON NSPS

Question 8 – Impact of proposed deferral mechanism on NSPs	
a) Would a six-month deferral of the payment of network charges present a material financial risk to NSPs? If so, are there ways of addressing or reducing these risks through the design of the deferral mechanism?	
b) Do NSPs have views on whether, in practice, the annual pricing proposal process would allow NSPs to recover any deferred revenue in the following regulatory year as described above? Are there any issues that may arise in seeking to utilise this process for this purpose?	
c) Do stakeholders have views on whether NSPs should be reimbursed for direct costs incurred as a result of the deferred payments and, if so, what would be the best mechanism for achieving this?	The DNSPs receive regulated income and will be able to recover the actual costs of providing the deferrals via their approved network determinations. EnergyAustralia believes this is the equitable and fairest way for any realised costs to be recovered.
d) If NSPs were to be reimbursed for their efficient costs (as well as recovering their total regulated revenue), do NSPs consider there would be any residual risk to their business arising from the deferral of network charges?	